

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF IDAHO

IN RE)	
)	Case No. 98-41095
KENNETH EARL CAIN and)	
CANDACE MELISSA CAIN,)	SUMMARY ORDER DENYING
)	DEBTORS' MOTION TO MODIFY
Debtors.)	INCOME TAX TURNOVER ORDER
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On May 13, 1999, Debtors filed a Motion to Modify Income Tax Turnover Order (the "Motion"). On June 15, the Court conducted a hearing on the Motion. The Chapter 7 Trustee, L.D. Fitzgerald opposed the Motion. On July 14, as authorized by the Court, Debtors filed the affidavit of Kenneth Earl Cain in support of the Motion.

Debtors filed for relief under Chapter 7 on September 11, 1998. In the Motion, Debtors seek to be excused from the provisions of this Court's Income Tax Turnover Order entered on the same day requiring them, among other things, to "turn over to the Trustee all income tax refunds now held or hereafter received by you for [1998]." Mr. Cain indicates in his affidavit that at the time of the filing of the bankruptcy petition, he resided in Idaho. However, after filing bankruptcy, Mr. Cain moved to Ohio. He attaches copies of his 1998 federal and Ohio state income tax returns filed in April, 1999. Mr. Cain states that the refunds he received, amounting to \$1,784 federal, and

\$370 state, are attributable to withholdings from his earnings from employment after moving to Ohio. Copies of W-2 statements attached to the returns attest to this fact. Therefore, Mr. Cain alleges that the tax refunds do not constitute property of the bankruptcy estate, and as a result, he should not be required to turn over the refunds to the Trustee.¹

The tax returns reveal, however, additional material facts. In addition to his Ohio earnings, Mr. Cain had a small amount of unemployment compensation and tax refund income. More importantly, though, Mr. Cain offset almost \$66,000 in net operating losses from his Idaho rental housing business against his income. As a result of these offsets, Mr. Cain had no taxable income for 1998, and thus was entitled to a refund of all withheld amounts.

It has long been the law that tax refunds attributable to the activities of the taxpayer occurring prior to the filing of the bankruptcy petition constitute property of the bankruptcy estate. 11 U.S.C. § 541(a); *Johnson v. Taxel (In re Johnson)*, 178 B.R. 216, 218 (9th Cir. B.A.P. 1995) (citing *Segal v. Rochelle*, 382 U.S. 375, 380 (1966)). Recently, the Ninth Circuit Bankruptcy Appellate Panel held that prepetition net operating losses and the tax refunds generated by claiming the corresponding deduction also

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Although authorized to do so, the Trustee filed no response to Mr. Cain's affidavit.

constitute property of the bankruptcy estate. *U.S. v. Towers (In re Feiler)*, 230 B.R. 164, 167 (9th Cir. B.A.P. 1999). Where a portion of the tax refund is attributable to facts or events occurring before the bankruptcy was filed, some sort of equitable apportionment of the resulting refund between the debtor and the bankruptcy estate is appropriate. *Towers v. Wu (In re Wu)*, 173 B.R. 411, 414 (9th Cir. B.A.P. 1994).

Debtors are correct in noting that the income from which the withholdings were made was earned by Mr. Cain after bankruptcy, and not property of the estate. 11 U.S.C. § 541(a)(6). However, the deductions claimed by Mr. Cain which provided, at least in part, a basis for the refunds were generated before the bankruptcy, or so it appears in the limited record before the Court.

For these reasons, **IT IS HEREBY ORDERED THAT** Debtors' Motion to Modify Income Tax Turnover Order be and is hereby **DENIED**. However, in the event the Trustee and Debtors cannot arrive at an equitable apportionment of the refunds, Debtors may renote this Motion for further evidentiary hearing.²

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The Court notes that on June 2, and again on June 25, 1999, Debtors filed an amended Schedule C claiming 75% of the Federal and Ohio refunds, respectively, exempt under Idaho Code § 11-207. No timely objection has been filed to the amended exemption claims, even though the claims seem inconsistent with the prior rulings of this Court. See *In re Pew*, 97.3 I.B.C.R. 76 (debtors' tax refunds do not constitute "earnings" or "disposable earnings" as those terms are used in Idaho Code § 11-207). The Court makes no decision concerning these amended exemption claims.

DATED This 4th day of August, 1999.

JIM D. PAPPAS
CHIEF U.S. BANKRUPTCY JUDGE

CERTIFICATE OF MAILING

I, the undersigned, hereby certify that I mailed a true copy of the document to which this certificate is attached, to the following named person(s) at the following address(es), on the date shown below:

Office of the U.S. Trustee
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David E. Rayborn, Esq.
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L. D. Fitzgerald
P. O. Box 6199
Pocatello, Idaho 83205

CASE NO.: 98-41095

CAMERON S. BURKE, CLERK
U.S. BANKRUPTCY COURT

DATED: August 4, 1999

By _____
Deputy Clerk